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MSN INDUSTRIES LTD.

Annual Report

FOR THE YEAR ENDED DECEMBER 31, 1970

Directors

W. A. ARBUCKLE, *Montreal*

W. S. BIRD, *Fredericton*

W. R. EAKIN, *Montreal*

K. J. FOWLER, *Huntsville, Ala.*

A. S. GORDON, *Montreal*

N. B. IVORY, *Montreal*

C. J. JACKSON, *Montreal*

Officers

C. J. JACKSON, *President*

G. R. DUNCAN, *Vice-President*

J. D. FLETCHER, *Secretary*

Subsidiaries

MUSSENS EQUIPMENT LTD.

MUSSENS SERVICE (1969) LIMITED

DORVAL DIESEL LTD.

COLBORNE ACCEPTANCE LIMITED

ONTARIO EQUIPMENT LIMITED

HOVERMARINE HOLDINGS LIMITED

MSN Industries Ltd., 1100 Norman St., Lachine, P.Q.

Annual Report to the Shareholders for the year ended December 31, 1970

Profit

Consolidated net profits of your Company after taxes for the year ended December 31, 1970 and after extraordinary items amounted to $597,362, equal to $1.17 per share. Consolidated net profits after taxes for the year ended December 31, 1970 and before extraordinary items amounted to $502,362, equal to 98.6 cents per share of the common stock outstanding. In the previous 9 month fiscal period ended December 31, 1969, consolidated net profits after taxes were $324,127 or 63.6 cents per common share. Earnings per share on a fully diluted basis for the year ended December 31, 1970 are 94 cents per share before extraordinary items, and $1.12 per share after extraordinary items, compared to 61 cents per common share for the 9 month fiscal period ended December 31, 1969. The dilution reflects the potential exercise of employee stock options in the gross amount of 25,000 common shares.

The 84% increase in earnings was the result of an improvement in the profit margin from 3.8% of sales in the prior period to 5.4% of sales during the year under review as well as the fact that reporting covers a full year's operations in 1970.

Operations

Total consolidated sales at $24,827,118 for the year represented an increase from the $21,119,997 recorded for the prior 9 month fiscal period. Sales volumes declined at Dorval Diesel, but due to improved sales mix and improved cost controls, this subsidiary recorded much higher net earnings.

In Mussens' Quebec and Labrador Branches sales tempo was up some 7 percent due to major increases in activity at both the Sept Iles and Quebec City Branches.

Sales and revenues and expenses of the Lachine Branch were lower in 1970, due to reduced construction activity in this area of the Company's operations.

Ontario Equipment Limited sales were down and net earnings substantially below the prior year due partly to reduced volumes and partly to reduced margins on certain classes of sales.

Colborne Acceptance Limited statements are shown separately in this report. Net income after taxes of $52,440 for the year ended December 31, 1970 compares favourably with net earnings of $39,840 for the previous 9 month fiscal period. The increase in the portfolio of leased vehicles continues to have an important impact on the earnings of this subsidiary.

Accounting Changes

In the Annual Report for the 9 month fiscal period ended December 31, 1969, an item called "Write off excess of cost over book value on purchase of H & C Equipment Co. Ltd." was treated as an adjustment to the Retained Earnings and this is now being restated on the Balance Sheet as "Excess of cost of investment in consolidated subsidiaries over book value of underlying net assets, less amortization". This change was made in order to conform with the statement presentation policy of the parent company, Danmont Corporation.

The acquisition during the year under review of Hovermarine Holdings Limited resulted in an additional excess of investment cost over underlying book value of $89,075.

The asset is being written off against earnings on a ten year amortization basis commencing the year after acquisition.

This accounting change has the effect of increasing the stated net shareholders' equity by $327,234, or 64.2 cents per share as at December 31, 1970, however this increase will be reduced by the amortization amount each year.

Industrial Relations

The three year agreement with the International Association of Machinists covering the Mussens bargaining unit at the Sept Iles Branch does not terminate until November 30, 1972.

The agreement with the UAW covering the Mussens' shop personnel at Lachine and Quebec City Branches and Dorval Diesel's Dorval location terminated November 8, 1970. Negotiations have just been completed for a new agreement to terminate November 8, 1973.

The agreement with the UAW covering office clerical staffs at Lachine and Dorval terminates May 31, 1971.

Financial

During the year under review, a total of $225,000 of the Company's debentures were purchased in the open market and lodged with the trustee for cancellation to meet sinking fund requirements. These were acquired at

prices which yielded the Company a discount advantage totalling $16,857.

Inventories

Consolidated Inventories at December 31, 1970 at $11,345,158 were down 2.6 percent from the $11,649,823 one year ago. Total consolidated parts inventories dropped by $181,537 during the year, however Dorval Diesel parts inventories increased by $139,300. Total consolidated equipment inventories decreased by $228,540, due to inventory reductions in Ontario Equipment Limited. Details on these inventories are included in the notes to the financial statements.

Corporate Planning and Development

Bucyrus-Erie Company have indicated their desire to adopt direct marketing of their line of mining equipment by the beginning of 1972. This corporate move by Bucyrus-Erie in no way affects our continuing representation of the commercial range of their equipment. While the loss of B-E mining equipment is significant, your Company is confident that its search for a replacement for the loss of these revenues will be successful.

During 1970 your Company acquired 55 percent of the common stock of Hovermarine Holdings Limited, a company with a wholly owned operating subsidiary, Hovermarine (Canada) Limited. Your Company also acquired 45 percent of the shares of Holdus Inc., an American company which holds 100 percent of the shares of Hovermarine Inc., of Texas. Hovermarine (Canada) Limited has been engaged in the production of prototypes of 2-3 passenger sports Hovercraft and extensive tests under varying conditions have been carried out with encouraging results. Further tests are presently being conducted in cooperation with the Department of National Defence. Some $150,000 in direct government grants through the PAIT and IRDIA programmes have been received in support of the research and development work conducted by Hovermarine (Canada) Limited.

Due to conflicting interests, your Company is forced by Detroit Diesel to dispose of the shares of Dorval Diesel Ltd. While this disposition will have an impact on the immediate corporate earnings, the substantial cash received will enable us to pursue other attractive acquisitions that could be compatible with our long-range corporate objectives.

During the year a number of prospective acquisitions were examined and negotiations conducted in a number of cases and those with merit are being continued. The Company is continuing its search for other possible acquisitions.

Outlook

Sales volume for the first two months of 1971 was greater than January and February last year. Government spending for public works, particularly in Quebec indicates a more active construction season. The construction of the new airport at Ste. Scholastique together with the requirement for access roads will utilize substantial quantities of the type of goods and services supplied by your Company. Highway work throughout the Province of Quebec is being significantly increased. The open pit mining expansion, particularly in the Gaspé region and the Labrador and Northeastern Quebec area serviced by our Sept Iles Branch will provide additional possibilities. As a consequence, your management is optimistic that it can develop an increase in business.

Your Directors extend their thanks to all Company personnel for their effective services during 1970.

On behalf of the Board of Directors.

C J Jackson

C. J. Jackson
President

March 26, 1971

Ten Year Financial Summary	1970 December 31	1969 December 31 (2)	1969*	1968*	1967*	1966*	1965*	1964*	1963*	1962*
			(Except for values per share all dollar amounts are stated in thousands)							
OPERATING RESULTS										
Sales	**24,827**	21,120	30,606	32,471	35,411	39,982	30,822	26,154	22,006	21,066
Depreciation	**96**	90	166	171	173	177	163	158	151	143
Interest on long-term debt	**258**	204	266	269	245	244	181	113	126	136
Income taxes	**610**	325	577	500	743	527	459	310	200	273
Net Profit (7)	**597**	324	560	461	611	645	524	370	215	277
Cash from operations (4)	**693**	414	726	632	784	822	687	528	366	420
SHAREHOLDERS' PARTICIPATION										
Shareholders' equity (8)	**6,508**	5,911	5,637	5,332	5,114	4,706	4,211	3,830	3,541	3,431
Dividends declared	—	51	255	242	204	228	164	82	122	113
Per common share (3)										
Cash from operations (4)	**1.36**	.81	1.42	1.24	1.54	1.61	1.39	1.08	.75	.87
Earnings (7)	**1.17**	.64	1.10	.90	1.20	1.27	1.06	.76	.44	.57
Dividends declared	—	.10	.50	.47½	.40	.44¾	.33	.16⅔	.25	23⅓
Equity (8)	**12.77**	11.60	11.06	10.46	10.03	9.24	8.53	7.82	7.23	7.10
No. of shares outstanding (3)	**509,595**	509,595	509,595	509,595	509,595	509,595	493,950	489,570	489,570	483,960
No. of shareholders (5)	**636**	655	739	814	879	809	326	326	325	328
BALANCE SHEET ITEMS										
Inventories	**11,345**	11,650	13,833	15,989	14,964	15,802	13,840	11,617	9,299	9,682
Working capital	**7,103**	6,272	7,305	7,261	6,612	6,342	5,325	3,747	3,932	3,995
Fixed assets (net)	**1,229**	1,313	1,642	1,548	1,525	1,685	1,307	1,288	1,189	1,023
Total assets (8)	**19,058**	20,424	21,671	23,774	23,310	24,247	21,764	19,748	14,720	15,728
Long-term debt (6)	**3,510**	3,756	3,915	4,072	3,560	3,784	2,814	1,500	1,651	1,751

*Fiscal year ended March 31.

(1) The finance subsidiary is carried at cost plus accumulated earnings.
(2) December 31, 1969 results are for a nine-month period for all companies except Ontario Equipment Limited which has contributed twelve months operation to these figures.
(3) Adjusted to reflect the three for one subdivision of shares, September 28, 1965.
(4) Cash from operations is net profit for year plus depreciation.
(5) Average number of shareholders during the year.
(6) Long-term debt excludes amount payable within one year.
(7) Including extraordinary item of $95,000 in 1970 — 18 cents per share.
(8) December 31, 1969, restated (note (4) to financial statements).

Consolidated Statement of Income and Retained Earnings

Year ended December 31, 1970 with comparative figures for the nine months ended December 31, 1969

	1970 Year ended December 31	1969 (note 4) 9 months ended December 31
Sales, including income from rentals and service and miscellaneous revenues	**$24,827,118**	21,119,977
Cost of sales, service, selling and general administrative expenses (note 11)	**23,514,679**	20,306,954
Operating income	**1,312,439**	813,023
Interest on long-term debt and amortization of debenture discount — net	**257,884**	203,736
Income before income taxes	**1,054,555**	609,287
Provision for income taxes:		
Taxes payable before reduction of $95,000 for losses of prior years brought forward (note 12)	**595,650**	326,500
Deferred	**14,350**	(1,500)
	610,000	325,000
Income before the undernoted	**444,555**	284,287
Net income of finance subsidiary	**52,440**	39,840
Minority interest in subsidiary's loss	**5,367**	—
Net income before extraordinary item	**502,362**	324,127
Extraordinary item, reduction of income taxes for losses of prior years brought forward (note 12)	**95,000**	—
Net income	**597,362**	324,127
Retained earnings at beginning of period	**5,480,408**	5,207,240
	6,077,770	5,531,367
Deduct dividends paid	—	50,959
Retained earnings at end of period	**$ 6,077,770**	5,480,408
Earnings per share:		
Income before extraordinary item	**$ .99**	.64
Extraordinary item	**.18**	—
	$1.17	.64
Fully diluted earnings per share (note 9):		
Income before extraordinary item	**$ .94**	.61
Extraordinary item	**.18**	—
Net income	**$1.12**	.61

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheet December 31, 1970 with comparative figures for 1969

Assets

	1970	1969 (Note 4)
Current assets:		
Cash	$ 39,331	33,263
Accounts receivable	3,695,556	4,461,649
Notes receivable	846,876	758,135
Inventories (note 2)	11,345,158	11,649,823
Prepaid expenses	71,743	74,421
Total current assets	15,998,664	16,977,291
Non-current portion of notes receivable	271,267	806,272
Funds held by a trustee for debenture holders	304,873	304,873
Investment in finance subsidiary not consolidated (note 1)	552,581	500,141
Advances to Hovermarine (Canada) Limited	—	127,120
Excess of cost of investments in consolidated subsidiaries over book value of underlying net assets, less amortization (note 4)	327,234	264,621
Other investment at cost	23,174	—
Fixed assets (note 3)	1,229,166	1,312,853
Research and development costs (note 5)	233,551	—
Unamortized debenture discount	115,861	130,485
Incorporation expense	1,861	—
	$19,058,232	20,423,656

See accompanying notes to consolidated financial statements.

On behalf of the Board:

N. B. Ivory, Director.
C. J. Jackson, Director.

	1970	1969 (Note 4)
Liabilities and Shareholders' Equity		
Current liabilities:		
Bank advances (note 6)	**$ 2,689,677**	3,127,991
Other loans payable (note 7)	**1,653,167**	1,528,383
Accounts payable and accrued expenses	**1,451,258**	2,085,964
Accounts payable — instalment payment basis (note 7)	**1,991,289**	2,862,481
Income taxes payable	**332,338**	144,490
Other taxes payable	**211,928**	181,989
Long-term debt due within one year	**246,320**	240,843
Due to finance subsidiary	**320,166**	533,224
Total current liabilities	**8,896,143**	10,705,365
Long-term debt (note 8)	**3,509,503**	3,755,823
Deferred income taxes	**27,700**	13,350
Discount on note of a subsidiary purchased at less than face value	**38,480**	38,480
Minority interest in subsidiary	**78,406**	—
Shareholders' equity:		
Capital stock (note 9):		
Cumulative redeemable preferred shares of $50 par value per share. Authorized 100,000 shares.		
Common shares of no par value. Authorized 1,000,000 shares; issued 509,595 shares — stated value	**430,230**	430,230
Retained earnings per accompanying statement (note 4)	**6,077,770**	5,480,408
Total shareholders' equity	**6,508,000**	5,910,638
Contingent liabilities (note 13)		
	$19,058,232	20,423,656

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of MSN Industries Ltd. and subsidiaries as of December 31, 1970 and the consolidated statements of income and retained earnings and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company and subsidiaries at December 31, 1970 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles which, except for the change with which we concur referred to in note 4 to the financial statements, were applied on a basis consistent with that of the preceding year.

PEAT, MARWICK, MITCHELL & CO.,
Chartered Accountants.

Montreal, Que.
February 3, 1971.

Notes to Consolidated Financial Statements December 31, 1970

1. Basis of consolidation:

The consolidated financial statements include all subsidiaries except a wholly owned finance company which is carried at equity value.

The consolidated statements of income and retained earnings and source and application of funds for the nine months ended December 31, 1969 include the consolidated results of operations and source and application of funds of Ontario Equipment Limited for the year ended December 31, 1969.

During the year the company acquired 55% of the issued shares of Hovermarine Holdings Limited, which is the parent company of Hovermarine (Canada) Limited. The financial statements of these companies as at and for the year ended December 31, 1970 are included in the consolidated financial statements.

2. Inventories:

	Basis of Valuation	**1970**	1969
New machines	Lower of cost (specific identification) or estimated realizable values as appraised by management	**$ 2,073,398**	2,327,512
Rental machines	Estimated realizable values (which are less than cost) as appraised by management	**4,652,512**	4,739,608
Used machines		**948,152**	835,482
Parts	Valued at suppliers' current list prices plus duty, less estimated dealers' discounts and allowance for obsolescence and price increases	**3,179,355**	3,360,892
Work in progress	Cost	**491,741**	386,329
		$11,345,158	11,649,823

3. Fixed assets:

	1970	1969
Buildings	**$ 805,430**	812,430
Shop and office equipment	**1,152,766**	1,091,365
Transportation equipment	**190,373**	296,781
Leasehold improvements	**143,492**	143,492
	2,292,061	2,344,068
Less accumulated depreciation and amortization	**1,306,061**	1,269,709
	986,000	1,074,359
Land	**243,166**	238,494
Net fixed assets	**$ 1,229,166**	1,312,853

Except for Ontario Equipment Limited, which owns approximately 15% of the fixed assets, depreciation is being computed at the following annual rates on a straight-line basis —

Buildings	2½%
Shop and office equipment	10%
Transportation equipment	20/25%

Ontario Equipment Limited calculates depreciation at the following rates on a diminishing-balance basis —

Buildings	5%
Shop and office equipment	10/20%

Leasehold improvements are being amortized over the term of the lease.

4. Excess of cost of investments in consolidated subsidiaries over book value of underlying net assets less amortization:

In 1969 the excess cost of $264,621 over the book value of the underlying net assets of a subsidiary acquired was written off by a charge to retained earnings. During 1970 this practice was changed to record the excess cost as an asset to be amortized on a straight-line basis over ten years commencing the year after the acquisition. The 1969 figures have been restated accordingly. Had the company not changed its accounting treatment, income for the year would have been increased by $26,462 and retained earnings at December 31, 1970 would have been reduced by $327,234.

The acquisition during the current year of Hovermarine Holdings Limited resulted in additional excess of investment cost over underlying book value of $89,075.

5. Research and development costs:

Development expenditures incurred by Hovermarine (Canada) Limited have totalled $385,512 on account of which $151,961 has been received in government grants.

6. Bank advances are secured by a general assignment of accounts receivable.

7. Other loans payable and accounts payable, instalment payment basis, are secured by machines included in inventory.

8. Long-term debt:

	1970	1969
Sinking fund debentures:		
6¼% Series "A" due February 1, 1972	**$ 210,000**	290,000
6¾% Series "B" due December 1, 1975	**400,000**	460,000
6½% Series "C" due July 2, 1984	**1,285,000**	1,325,000
6¼% Series "D" due July 2, 1985	**875,000**	900,000
7½% Series "E" due September 1, 1987	**690,000**	710,000
	3,460,000	3,685,000
Mortgages:		
5½% due October 1, 1976	**57,500**	67,500
8% due November 1, 1988	**238,323**	244,166
	3,755,823	3,996,666
Less amount due within one year	**246,320**	240,843
	$3,509,503	3,755,823

9. Options to purchase Capital Stock:

In accordance with a share option plan for officers and key employees, excluding directors, there are 25,000 common shares reserved for options exercisable at $4.00 per share at various dates to December 31, 1974.

10. Contractual obligations:

The company premises in Montreal and Sept Iles are occupied under long-term net leases of varying terms to 1989, requiring annual rental payments of $123,000. Under the terms of these leases the company has options to purchase the properties.

11. Expenses include:

	1970	1969
Depreciation and amortization of fixed assets	**$ 96,086**	90,088
Amortization of excess of cost of investments in subsidiaries over underlying book values	**26,462**	—
Directors' remuneration — from MSN Industries Ltd.	**2,700**	3,875
— from Mussens Equipment Ltd.	**3,800**	950
Officers' remuneration — from MSN Industries Ltd.	**—**	77,088
— from Mussens Equipment Ltd.	**264,992**	98,182
— from Ontario Equipment Limited	**22,200**	20,400
	$ 416,240	290,583
Number of directors (2 past directors)	**9**	9
Number of officers (8 past officers)	**11**	11
Number of officers who are directors (1 past officer)	**2**	3

12. Income taxes payable will be reduced as a result of a subsidiary applying losses of prior periods against current taxable income. The resulting reduction in income taxes payable has been shown as an extraordinary item, as recommended by The Canadian Institute of Chartered Accountants. Losses incurred by subsidiary companies, which may be carried forward to reduce future taxable income of those subsidiaries as allowed by the Income Tax Act, amount to $392,000. This amount is not recorded in the consolidated accounts.

13. Contingent liabilities:

The company is contingently liable for:

Customers' lien notes discounted	$3,278,000
Legal action — which in the opinion of legal counsel has been prescribed	240,000
Guarantee of finance subsidiary bank loan	732,000
	$4,250,000

14. Transactions originating in U.S. currency have been recorded at exchange rates in effect at the time of the transactions and liabilities in U.S. funds at December 31, 1970 have been translated to Canadian dollars at the rate of exchange at that date.

Consolidated Statement of Source and Application of Funds

Year ended December 31, 1970 with comparative figures for the nine months ended December 31, 1969

	1970 Year ended December 31	1969 (note 4) 9 months ended December 31
Funds provided:		
From operations:		
Net income	$ 597,362	324,127
Add depreciation, amortization and other items not affecting working capital	147,180	112,617
Funds provided from operations	744,542	436,744
Decrease in non-current receivables	535,005	17,143
Proceeds from sale of fixed assets	31,732	327,477
Working capital at date of acquisition of subsidiaries	1,757	(97,979)
Total funds provided	1,313,036	683,385
Used as follows:		
Purchase of fixed assets	37,640	93,949
Dividends paid	—	50,959
Repayment of long-term debt	246,320	159,426
Increase in investment of unconsolidated finance subsidiary	52,440	39,840
Investment in subsidiary and affiliated companies	35,174	133,520
Investment in non-current notes receivable	—	806,272
Proceeds on sale of fixed assets lodged with Trustees for debenture holders	—	304,873
Advances to Hovermarine (Canada) Limited	—	127,120
Increase in research and development costs of Hovermarine (Canada) Limited	105,500	—
Minority interest portion of loss of a subsidiary	5,367	—
Total funds used	482,441	1,715,959
Increase (decrease) in working capital	$ 830,595	(1,032,574)

See accompanying notes to consolidated financial statements.

Colborne Acceptance Limited

Balance Sheet December 31, 1970 with comparative figures for 1969

	1970	1969
Assets		
Cash	$ 79,221	46,302
Notes and accounts receivable:		
Maturing within one year	850,592	208,764
Maturing after one year	40,403	342,935
	890,995	551,699
Less deferred income	111,623	84,584
Net receivables	779,372	467,115
Income and special refundable taxes recoverable	—	1,525
Due from affiliated companies	320,166	533,224
Rental fleet, at cost less depreciation:		
Automobiles and trucks	195,977	109,038
Less accumulated depreciation	64,244	20,241
Net rental fleet	131,733	88,797
	$1,310,492	1,136,963
Liabilities and Shareholders' Equity		
Bank loan (secured by notes and accounts receivable)	$ 732,000	627,000
Income taxes payable	15,991	2,940
Sales tax payable	198	—
Deferred income taxes	9,722	6,882
Shareholders' equity:		
Capital stock:		
6% non-cumulative redeemable preferred shares of $10 par value per share. Authorized 16,450 shares.		
Common shares of no par value. Authorized 241,500 shares; issued 100,000 shares	100,000	100,000
Retained earnings — per accompanying statement	452,581	400,141
Total shareholders' equity	552,581	500,141
	$1,310,492	1,136,963

On behalf of the Board:
C. J. JACKSON, Director.
G. R. DUNCAN, Director.

Statement of Income and Retained Earnings

	Year ended December 31	9 months ended December 31
Income:		
Interest earned	$ 128,587	104,642
Rental revenue	62,763	24,069
	191,350	128,711
Expenditure:		
Interest on loans	46,493	40,603
Administration charge	1,000	750
General expenses and bank charges	4,839	3,809
Depreciation	44,003	18,307
Loss on disposal of automobiles and trucks	75	902
	96,410	64,371
Income before income taxes	94,940	64,340
Provision for income taxes:		
Currently payable	39,660	22,207
Deferred	2,840	2,293
	42,500	24,500
Net income	52,440	39,840
Retained earnings at beginning of period	400,141	360,301
Retained earnings at end of period	$ 452,581	400,141

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the balance sheet of Colborne Acceptance Limited as of December 31, 1970, and the statement of income and retained earnings for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the company at December 31, 1970, and the results of its operations for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding period.

PEAT, MARWICK, MITCHELL & CO.,
Chartered Accountants.

Montreal, Que., January 21, 1971.

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